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Sustainable insurance

Recent trends on ESG for the insurance sector

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Today's speakers

Michael Wagemans
Head of sustainability
mwagemans@kpmg.com
+32 3 821 17 14

Walter Jacob
Senior Counsel
wjacob@kpmglaw.be
+32 2 708 38 11

Michiel Dobbelaere
Senior Manager Advisor
mdobbelaere@kpmg.com
+32 2 708 41 75

Dieder Moelans
Director
diedermoelans@kpmg.com
+32 2 708 38 03

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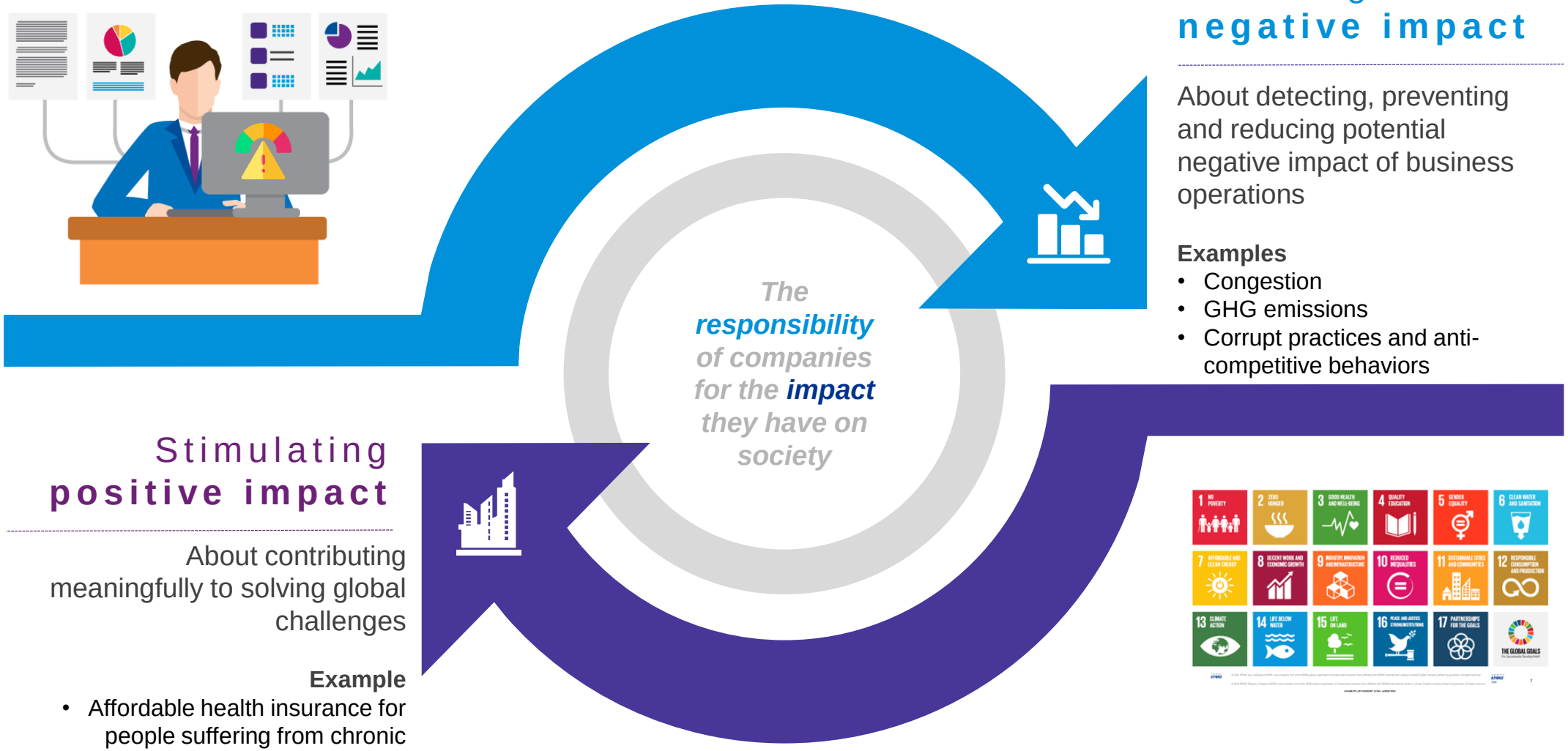
Sustainability / ESG - The bigger picture

With speaker Michael Wagemans

Sustainability. What is it about?



Reducing negative impact

About detecting, preventing and reducing potential negative impact of business operations

Examples

- Congestion
- GHG emissions
- Corrupt practices and anti-competitive behaviors

Stimulating positive impact

About contributing meaningfully to solving global challenges

Example

- Affordable health insurance for people suffering from chronic diseases

Why act now? We are in the perfect storm!

Consumers

Sustainability increasingly features in purchase decisions.

Example – Growing interest (and scrutiny) of pension saving funds tilted towards sustainability.

Financial community

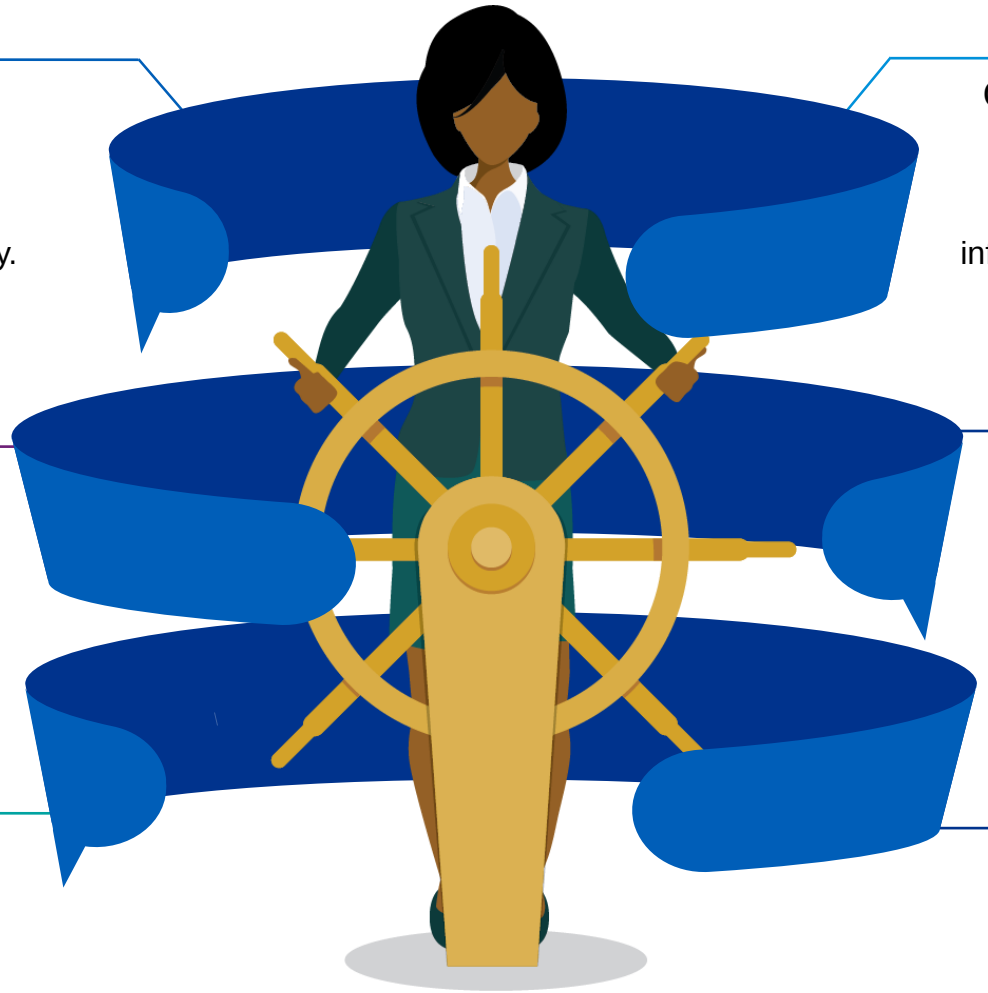
Investment appetite is shifting to ESG / sustainability.

Example – Sustainability-linked financial instruments are becoming mainstream.

Authorities

Regulatory complexity regarding sustainability increases.

Example – Regulatory initiatives, such as Corporate Sustainability Reporting Directive (CSRD) and EU Taxonomy.



Business partners

Greater demand to improve sustainability of value chains.

Example – Demands for ecosystem-related information, e.g. environmental standards at body repair shops in the context of car insurance offering.

Employees

Sustainability has become a vital flank in 'the war for talent'.

Example – Young graduates prefer to work for a company that has a positive impact on the world.

Civil society

Stakeholder capitalism is in vogue.

Example – Civil society is calling companies to account on important topics, such as diversity & inclusion.

There has been an evolution in the way companies engage sustainability

RISK MITIGATION

Avoiding downsides due to cost increases, market share loss or fines driven by regulation or market consensus.

Example

Risk of non-renewal of operating license in case of non compliance to environmental concerns.

COST REDUCTION

Improving cost position through operational efficiency with company's internal scope (e.g. energy, waste, water, ...).

Example

Using IoT devices and software to monitor real-time data about buildings for cost-efficient property management.

NEW MARKETS

Creating value from product / service innovations, new markets, and commercial validation of sustainability efforts (e.g. charge premium, preferred partner position).

Example

Products catering to the un(der)insured. Building ecosystems with partners to provide value-add services.

REPUTATION & OTHER BENEFITS

Capturing extended reputation benefits from sustainability (e.g. employee engagement, brand enhancement, ...).

Example

"Sustainability is an increasingly important factor in attracting and managing talents. With top talent in short supply, more companies take sustainability seriously, yielding better business results" – Harvard Business Review.

Tackling sustainability in business through engagement of ESG-factors or ESG incorporation/integration

ESG is short for Environmental, Social, and Governance

ESG includes a constellation of **sustainability-related themes** and corresponding **non-financial performance indicators** to assess:

- The viability of a business
- The impact of the company's products, services and business practices on the planet and society

ESG factors are recognized as representing significant **financial risks and opportunities**

There is a push towards **ESG integration / incorporation**

A snapshot of ESG factors

Environmental

- Emission to air, land, and water
- Energy consumption: Direct with Fuels/Indirect with Electricity
- Energy efficiency strategy and carbon management
- Use of water, especially in water scarce regions
- Use of raw materials
- Use of scarce resources
- Sourcing practices such as the use of responsibly sourced materials
- Management of waste and recycling
- Impacts on ecosystems and biodiversity (e.g. deforestation and the use of pesticides)
- Exposure to extreme weather
- Readiness to respond to changing regulations on environmental performance

Social

- Worker safety
- Employee demographics
- Employee attraction/retention records
- Approach to diversity and equal opportunities
- Level of customer satisfaction
- Protection of customers' data and compliance with privacy laws
- Approach to human rights risks, such as labor standards, child labor and modern slavery
- Strength of relationships with workers and communities
- Supply chain risks, such as standards of working conditions in the supply chain
- Appropriate and lawful use of marketing communications
- Product safety records

Governance

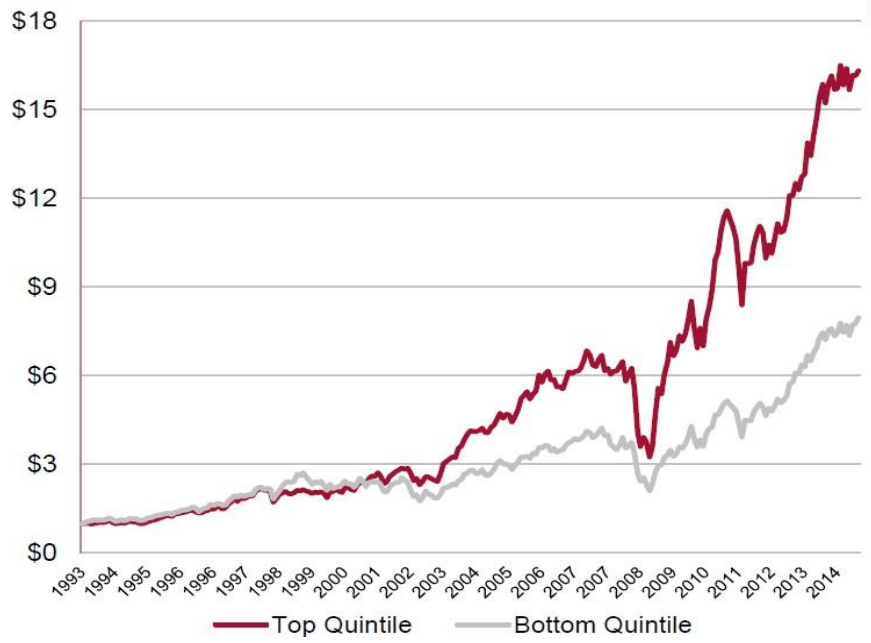
- Executive remuneration and demographics
- Board remuneration and demographics
- Compliance with accounting standards
- Examples of anti-competitive behavior
- Audit Committee and Board structure
- Bribery, corruption, and responsible tax record
- Succession planning
- Lobbying record and political contributions
- Robustness of ESG risk management processes
- Presence of appropriate whistleblower and grievance mechanism

ESG is a very dynamic space that continues to evolve

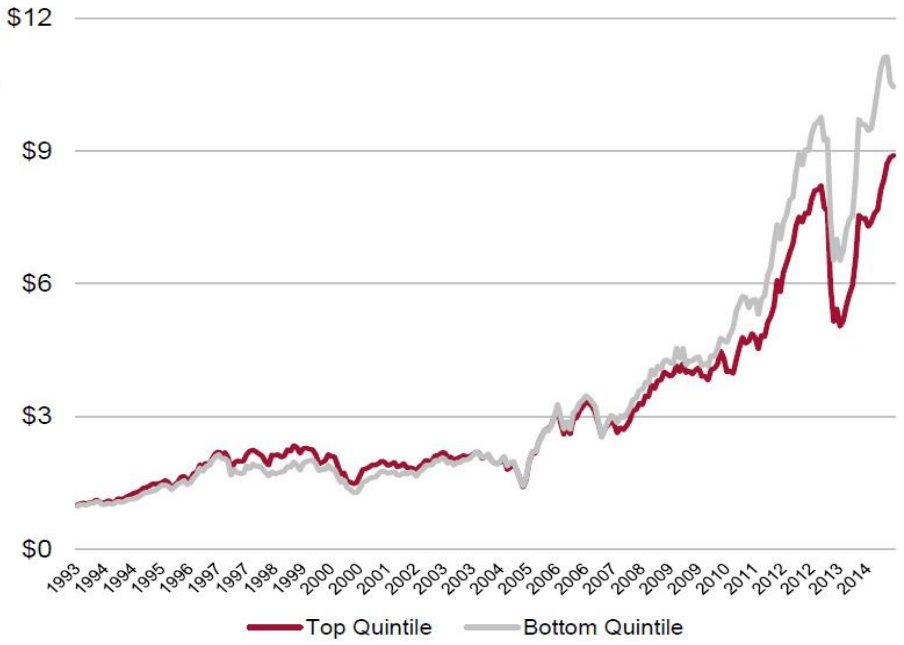
ESG incorporation contributes to superior financial performance

Companies with good performance on *material ESG* issues significantly outperform firms with poor performance on these issues. Further, firms with good performance on ESG issues not classified as material do not underperform firms with poor performance on these same issues

Material ESG issues



Immaterial ESG issues



Source: Mo Khan, George Serafeim and Aaron Yoon (2015), Corporate Sustainability: First Evidence on Materiality. The Accounting Review

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The emerging regulatory framework

With speaker Walter Jacob

Focus of the regulation

EU Action Plan on Sustainable Finance

Goals:

- Reorientation of funds flow towards a sustainable economy
- Focus on sustainability in the context of risk management
- Improve transparency and long-termism

Core components:

- EU Taxonomy
- EU Green bond standard
- Low-carbon benchmarks
- Regulation concerning sustainable investments and sustainability risks
- Guidelines on reporting of climate-related information

Links to:

- Non-Financial Reporting Directive (NFRD)
- Sustainable Finance Disclosure Regulation (SFDR)
- ESG-related changes in Solvency II, IDD, MiFID II, AIFMD, UCITS-D, etc.
- TCFD recommendations

10 Actions of EU Sustainable Finance Action Plan

#1 ESTABLISHING AN EU CLASSIFICATION SYSTEM FOR SUSTAINABILITY ACTIVITIES

#2 CREATING STANDARDS AND LABELS FOR GREEN FINANCIAL PRODUCTS

#3 FOSTERING INVESTMENT IN SUSTAINABLE PROJECTS

#4 INCORPORATING SUSTAINABILITY WHEN PROVIDING INVESTMENT ADVICE

#5 DEVELOPING SUSTAINABILITY BENCHMARKS

#6 BETTER INTEGRATING SUSTAINABILITY IN RATINGS AND RESEARCH

#7 CLARIFYING INSTITUTIONAL INVESTORS AND ASSET MANAGERS' DUTIES
(ESG in investment process + disclosures on it)

#8 INCORPORATING SUSTAINABILITY IN PRUDENTIAL REQUIREMENTS

#9 STRENGTHENING SUSTAINABILITY DISCLOSURE AND ACCOUNTING RULE-MAKING

#10 FOSTERING SUSTAINABLE CORPORATE GOVERNANCE AND ATTENUATING SHORT-TERMISM IN CAPITAL MARKETS

Key action point : EU Taxonomy

EU Taxonomy

What is the impact?

- **Classification system** to help identify sustainable economic activities.
- Transparency tool that will introduce mandatory disclosure obligations on some companies and investors, requiring them to disclose their share of Taxonomy-aligned activities.
- Planning tool for companies, who can reliably use the EU Taxonomy to plan their climate and environmental transition and raise finance for this transition.
- Financial companies, if they wish, can use the EU Taxonomy to design credible green financial products.
- Specific disclosure requirements and templates for **insurance and reinsurance companies** under the art. 8 Delegated Regulation (cf. art. 7 and annexes IX, X and XI).
- Specific KPI's **related to investments** and **underwriting activities**.

What is the status?

- **Q2 2021**: Publication of the so-called **Climated Delegated Regulation** and of the **art. 8 Delegated Regulation**.
- **Dec. 2021**: Expected publication of the **remaining 4 delegated regulations** regarding environmental objectives relating to (i) protection of water and marine resources, (ii) transition to a circular economy, (iii) pollution prevention and control and (iv) protection and restoration of biodiversity and ecosystems.
- **Q1 2022**: Taxonomy companies under the NFRD will be required to disclose in the course of 2022 on activities relating to **climate change mitigation and climate change adaptation**.
- **Q1 2023**: Taxonomy companies under the NFRD will be required to disclose in the course of 2023 on activities related to **all environmental objectives**.

Key action point : Sustainable Finance Disclosure Regulation

Sustainable Finance Disclosure Regulation (SFDR)

What is the impact?

- Regulation imposes on **financial market participants** (e.g. **insurance companies offering IBIPs**) and **financial advisers** (e.g. **insurance intermediaries**) the obligation to disclose the following information:
  - ✓ How **sustainability risks** are integrated in the investment/advice process;
  - ✓ Whether **negative externalities** on environment and social justice of the investment decisions/advice are taken into consideration and, if so, how this is reflected at the product level;
  - ✓ Other sustainability-related information (incl. environmental sustainability information as per the Taxonomy Regulation).
- Impact on
  - ✓ policies and procedures
  - ✓ website
  - ✓ pre-contractual information
  - ✓ periodic reporting

What is the status?

- **10 March 2021**: **Entry into force of the majority of provisions** relating to disclosures via website and pre-contractual information.
- **30 June 2021**: **Principal adverse sustainability impacts** of investment decisions on sustainability factors for FMPs >500 employees.
- **1 January 2022:** **enhanced disclosure requirements** on products promoting E/S characteristics or on sustainable investments (at product level) regarding climate change mitigation / adaptation
- **1 January 2023:** **enhanced disclosure requirements** on products promoting E/S characteristics or on sustainable investments (at product level) for remaining objectives.

Key action point : Insurance distribution & governance

Insurance distribution & governance processes

➢ What is the impact?

- **Sustainable Finance Package (April 2021):**
  - ✓ **Integration of sustainability risks (factors / objectives preferences) in:**
    - ❑ Customer suitability assessment for IBIPs (top up to existing rules) (incl. ranking / grouping products based on the degree of sustainability)
    - ❑ Product Oversight & Governance Process
    - ❑ Internal governance processes (notably conflicts of interest)
  - ✓ Commission Delegated Regulation amending Delegated Regulations (EU) 2017/2358 and (EU) 2017/2359 as regards the **integration of sustainability factors, risks and preferences into the product oversight and governance requirements for insurance undertakings and insurance distributors** and into **the rules on conduct of business and investment advice for insurance-based investment products.**
  - ✓ Commission Delegated Regulation amending Delegated Regulation (EU) 2015/35 as regards the **integration of sustainability risks in the governance of insurance and reinsurance undertakings**

➢ What is the status?

- **April 2021:** Publication of the sustainable finance package (still in draft format)
- Application **12 months following official publication** in the EU O.J.

Key action point : NFRD => CSRD

NFRD ➔ CSRD

➢ What is the impact?

- **Extended scope**: All [listed or non-listed] large companies (> 250 employees; EUR 40 mln turnover; EUR 20 mln total assets – 2 out of 3 criteria)
- All other (small/medium) listed companies (get extra 3 years to comply)
- **Sustainability information** to be included in the Management Report. Management Report proposed to include separate Sustainability Statements. To be submitted in Electronic format.
- **Reporting should include:**
  - ✓ Reporting on impacts by the company on the environment as well as risks on the company by the environment
  - ✓ Climate change to be included
  - ✓ Process for selecting most relevant risks and impacts
  - ✓ Forward looking information, including strategy, targets, progress
  - ✓ Information on intangibles (social, human & intellectual capital)
  - ✓ Reporting in line with EU Taxonomy, SFDR and EU Sustainability Reporting Standards

➢ What is the status?

- Proposal Corporate Sustainability Reporting Directive, **implementation by FY 2023**
- First set of Sustainability Reporting Standards, **implementation by FY 2023**
- Second set of Sustainability Reporting Standards, **implementation by FY2024**

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Practical implementation SFDR & ESG IDD

With speaker Michiel Dobbelaere

SFDR Implementation

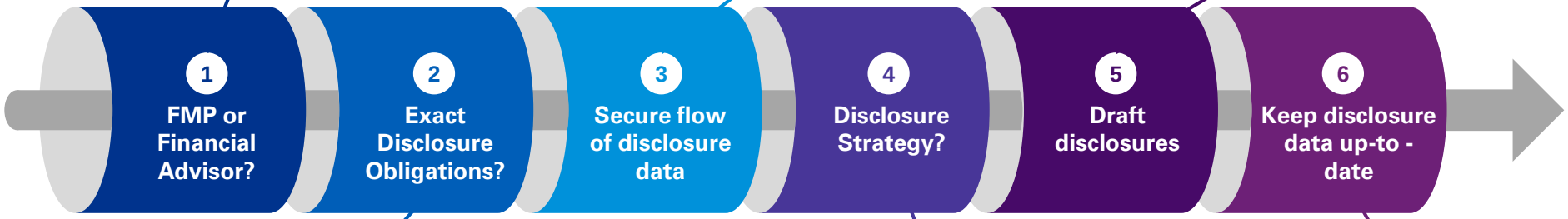
Channel	Disclosure obligation	FMP	FA	Ref. + Date	Firm / Product Level
Website	Information about the firm's **policies on integrating sustainability risks** in their investment / advice process	X	X	**Art. 3 SFDR** 10.03.2021	
	Principal adverse sustainability impacts of investment decisions on sustainability indicators	X	X	**Art. 4 SFDR** 10.03.2021 / 30.06.2021	
	Integration of sustainable risks in **remuneration policy**	X	X	**Art. 5 SFDR** 10.03.2021	
	Additional disclosure for **products promoting E/S characteristics** and **sustainable investments**	X	/	**Art. 10 SFDR** 10.03.2021	
Pre-contractual disclosure	Pre-contractual information on the integration of **sustainability risks**	X	X	**Art. 6 SFDR** 10.03.2021	
	Principal adverse sustainability impacts of investment decisions on sustainability factors	X	/	**Art. 7 SFDR** By 30.12.2022	
	Enhanced disclosure on **E/S characteristics** + Taxonomy Disclosures	X	/	**Art. 8 SFDR** 10.03.2021 1.01.2022/23	
	Enhanced disclosure on **sustainable investments** + Taxonomy Disclosures	X	/	**Art. 9 SFDR** 10.03.2021 1.01.2022/23	
Periodic reports	Enhanced disclosure on how **E/S characteristics** are met + Taxonomy Disclosures	X	/	**Art. 11 SFDR** 1.01.2022 1.01.2022/23	
	Enhanced disclosure on the sustainability-related impact of the **sustainable investments** + Taxonomy Disclosures	X	/	**Art. 11 SFDR** 1.01.2022 1.01.2022/23	

SFDR Implementation

- Define which of your insurance **products are in scope** of the SFDR
- Define for each in scope product whether you act as **Financial Market Participant** (FMP) or as **Financial Advisor** (FA)

- For each disclosure you must ensure that the necessary data will be **available**
- Secure its **continuous flow** (e.g. contractual obligation for portfolio managers, EMT, investment fund disclosures, data providers, …)

- **Draft** actual disclosures
- Have them **approved** by different boards, stakeholders and committees

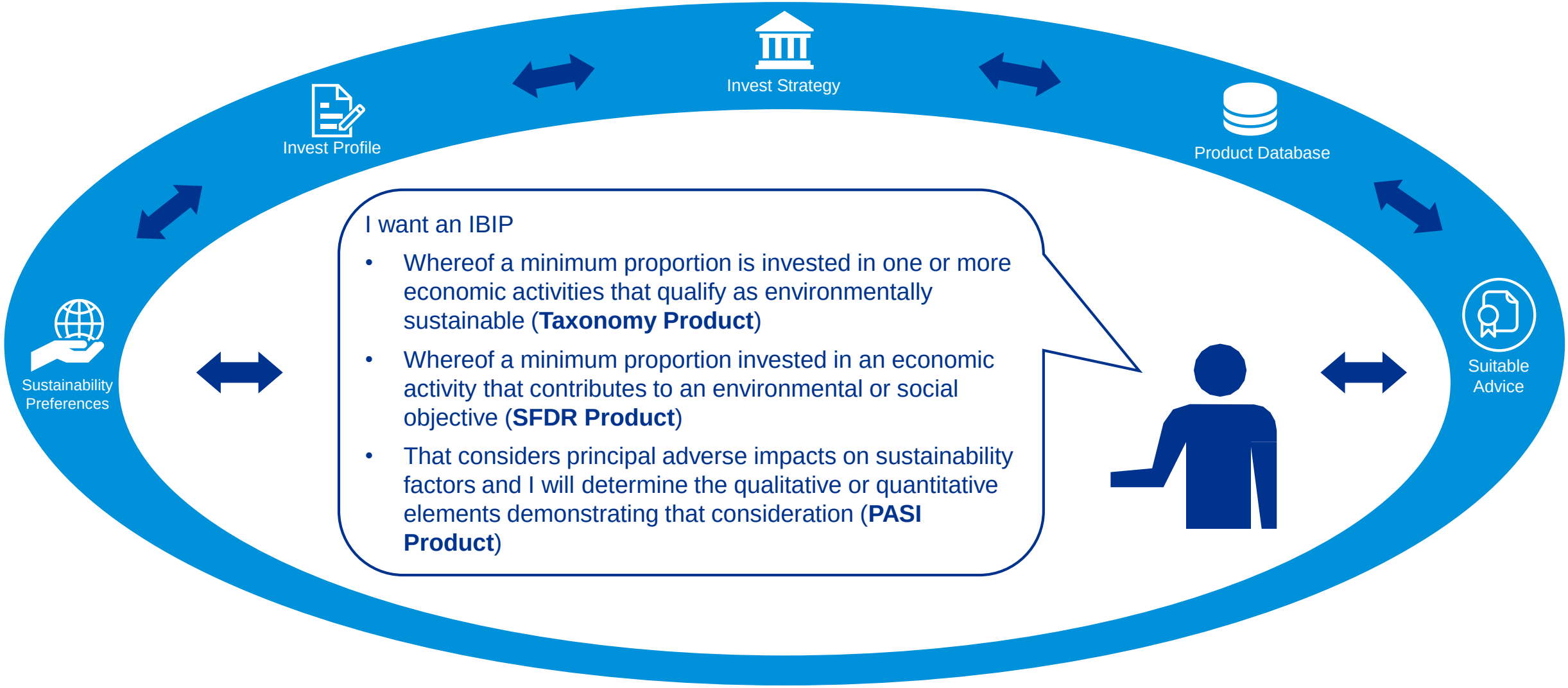


- Define your disclosure obligations **at firm level**
- Define your disclosure obligations **at product level**
- Define exact **deadline** for each disclosure
- Potentially take into account distribution network (independent brokers?)

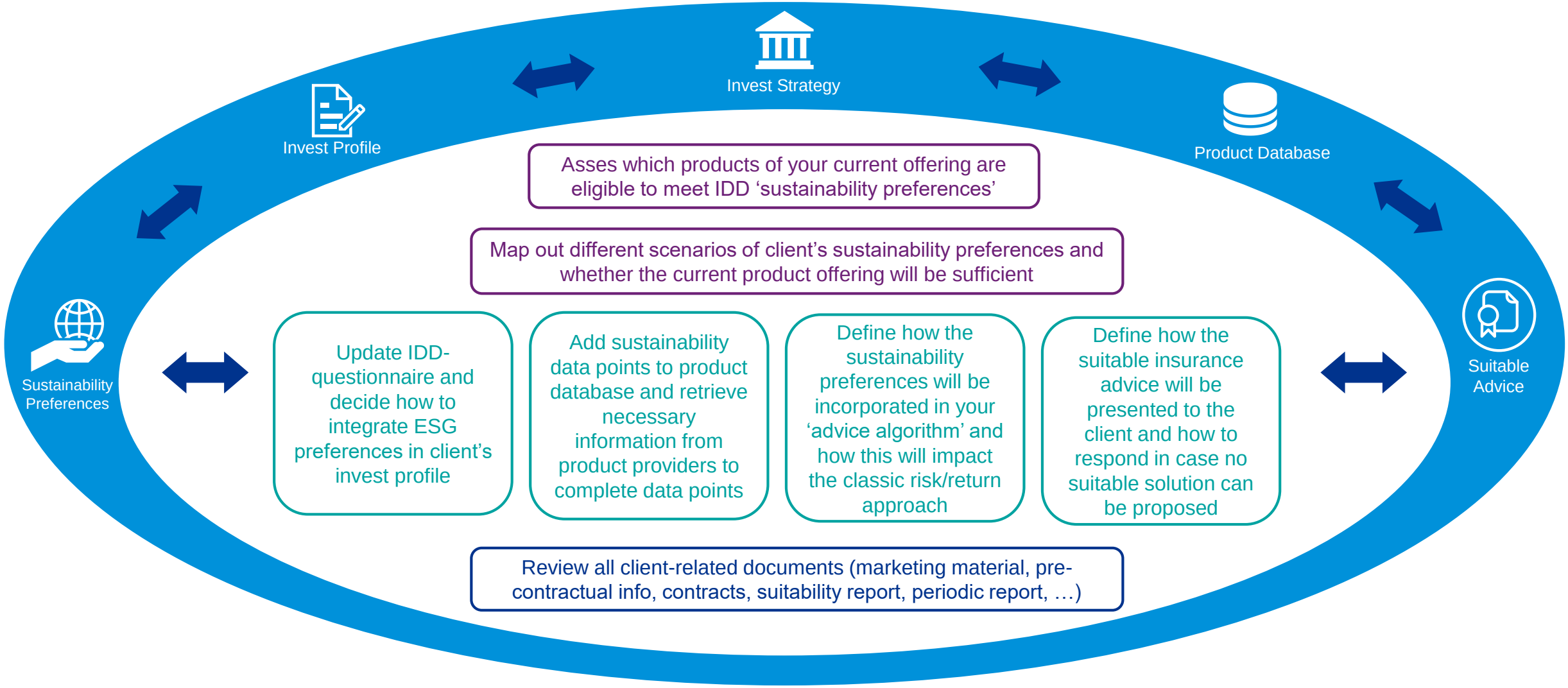
- Align with **overall sustainability strategy** of the firm
- Decide which disclosures are going to be made (potential **opt-out**)
- Define **exact disclosure places** (where on the website, which exact pre-contractual docs and periodic reports, …)

- Define **update and review terms** for each disclosure
- Integrate sustainable finance disclosures into **existing document generation** processes (e.g. periodic report)
- Install **periodic review processes** for more static data (e.g. firm level disclosures)

ESG Preferences



ESG Preferences



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Impact Solvency II Risk Management (ORSA)

With speaker Dieder Moelans

Impact on SII Risk Management

The European Commission has published a draft Delegated Regulation amending the Delegated Regulation, specifying a.o. that undertakings should integrate sustainability risks in their risk management.

Two recent publications (focusing on climate risks):

- Opinion of EIOPA to National Supervisory Authorities (April 2021) regarding the use of climate change risk scenario's in the ORSA;
- IAIS publication (May 2021): Application paper on the supervision of climate-related risks in the insurance sector.

Opinion of EIOPA includes (among others) the following expectations:

- Within the ORSA: assessing material climate change risk exposures (qualitatively and quantitively), on short term, mid-term and long-term;
- At least two long-term climate scenario's should be considered

  EIOPA mentions a global average temperature increase < 2°C (and preferably < 1,5°C) versus a scenario in which the temperature increase > 2°C
- EIOPA will start monitoring the application of the opinion by the national supervisory authorities in 2023

Different kinds of risks should be analysed, togher with the impacts and development of a risk framework

Impact on SII Risk Management

Sustainability/ESG is encompassing more than just climate risks

➔ focus should hence not only be on climate-related risks within the business and risk management.

A few examples linked to the 'S' Letter *('Social'):*

➔ *a source of both challenges and opportunities in the short and the long run.*

e.g. evolving societies creating new insurance needs:

- Fair and transparent product ("Value for money", clear wording of the coverage, cost structure,…)
- New ways of living (mobility, digitalization, …)
- Demographic trends (pension, health care,…)
- Diversity and inclusion (providing coverage to policyholders with limited resources,…)

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